



Special Series on COVID-19

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Government Support to State-Owned Enterprises: Options for Sub-Saharan Africa

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Some state-owned enterprises are facing significant financial distress during the pandemic and economic crisis. Some operate in core sectors of the economy and provide basic services and may need support to avoid collapse, raising the question whether governments should provide temporary exceptional financial assistance. This note discusses guiding principles to help decide when countries should intervene to help these companies, and how this support can be done given the financial constraints of governments. It is also imperative that governments strengthen oversight and firm governance to ensure public resources are well used. While the focus on this note is on Africa, these principles are applicable across other regions.

I. STATE-OWNED ENTERPRISES IN SUB-SAHARAN AFRICA

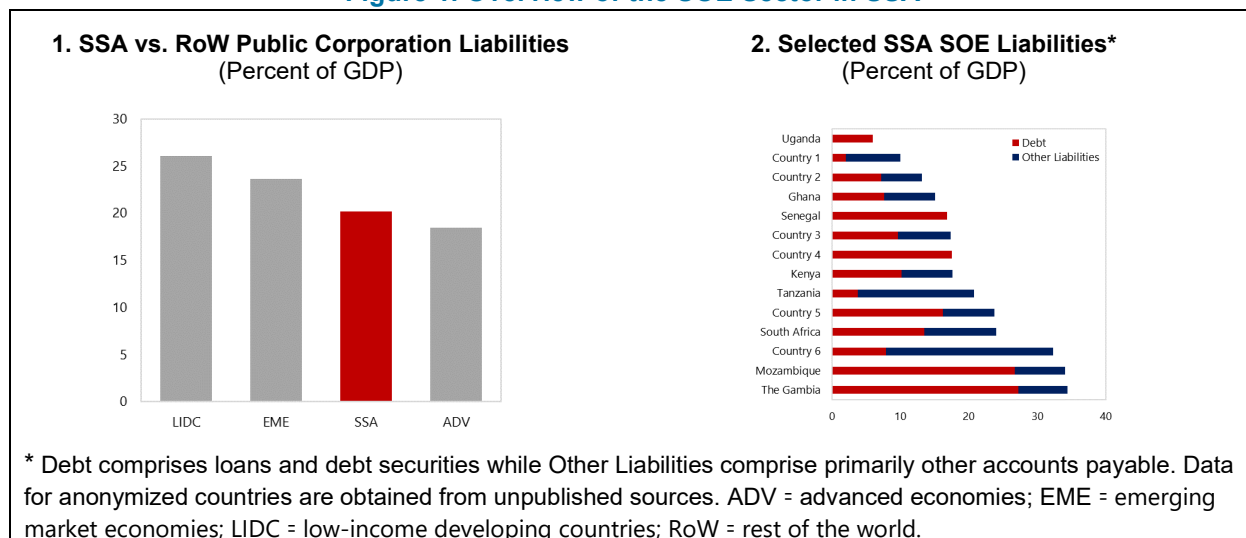
The state-owned enterprise (SOE) sector in sub-Saharan Africa (SSA) has systemic implications for the public finances and the economy more broadly.¹ Across a subset of SSA countries, SOEs account for a significant share of public sector balance sheets (PSBSs), with liabilities worth an average of 20 percent of GDP, and assets of about 32 percent of GDP (Figures 1a and 1b).² For the sample of countries for which data are available, SOE revenues average 7 percent of GDP, expenditure 8 percent of GDP, and losses are about 1 percent of GDP. SOEs also contribute significantly to government revenue in some countries.

¹ For the purposes of this note, SOEs refer to entities that would be considered public corporations under the criteria set out by the IMF's [Government Finance Statistics Manual 2014](#), as distinct from parastatal entities which might be constituted in a legal form resembling SOEs but which are in fact performing government functions. Where such parastatals are financed through their own revenue, they are also likely to face financial difficulties arising from COVID-19. These difficulties are best addressed through the budget.

² Average for the 14 countries for which data are available in the IMF's [PSBS Database](#), [Fiscal Transparency Evaluations \(FTEs\)](#) and [Capacity Development \(CD\)](#) reports. Data exclude central banks and are largely nonfinancial corporations. For these countries, on average, SOEs account for 21 percent of public sector liabilities and 34 percent of assets.

SOEs are concentrated in essential and strategic sectors. In most SSA countries, SOEs play an important role in providing basic services such as electricity (generation, transmission, and distribution), water, telecommunications, and other public utilities. SOE failures in these sectors would likely result in systemic problems for the economy and affect efforts to contain the spread of COVID-19. Additionally, SOEs are often a key player in strategic sectors. These include extraction and processing of natural resources, operation of strategic infrastructure such as airports and ports, provision of transport services such as national airlines and railways, and purchase and resale of agricultural commodities. In some cases, SOEs occupy a monopoly market position, and are often an important source of employment. SOEs also play a significant role in public investment and accounted for 31 percent of infrastructure project investment in 2017 for SSA.³

Figure 1. Overview of the SOE Sector in SSA



Source: IMF staff estimates.

Many SOEs already faced difficult financial conditions before the pandemic. A number of SOEs across SSA were in financial distress long before the onset of COVID-19. Many are persistently unprofitable and face liquidity constraints, giving rise to a need for sustained and significant bailouts (Annex 1). In some cases, these financial difficulties are exacerbated by the SOEs carrying costly public policy mandates for which they are uncompensated. As a result, SOEs have become an important source of fiscal risks (Annex 2). The challenges faced by the sector are compounded by COVID-19, which brought a 5.2 percentage point downward revision in the 2020 SSA growth outlook from the October 2019 forecast.⁴ That said, not all SOEs are unprofitable and some do have the potential to be profitable and make a positive contribution to the public finances and the economy more broadly. Some SOEs can also be profitable even under adverse macroeconomic circumstances.

II. EXCEPTIONAL GOVERNMENT SUPPORT TO SOES DURING THE PANDEMIC: WHEN AND HOW?

SOEs have been used by governments to help manage crises, including the pandemic. For example, state-owned utilities are providing water and electricity, including in some cases at subsidized prices (e.g., Ghana) and allowing deferred payments to households and firms. Public banks are being asked to provide loans to families and micro-, small-, and medium-sized firms in many countries.

³ World Bank and PPIAF. 2017. "Who Sponsors Infrastructure Projects, Really? Disentangling Public and Private Contributions."

⁴ IMF. 2020. *Regional Economic Outlook: Sub-Saharan Africa*, April.

However, some SOEs may face significant financial distress during the crisis, raising the question of when and how government should provide support. Governments may decide to intervene to provide liquidity or address solvency issues to strategic SOEs such as utilities and with them entire sectors of the economy. However, cash-strapped governments with weak balance sheets in low-income countries will struggle to provide financial support to their SOEs. The support will also need to be well designed and targeted to the present crisis to avoid giving bailouts to cover inefficiencies and mismanagement.

This section discusses the main trade-offs that governments will need to consider when deciding when to intervene and how to do it. The focus of this analysis is on nonfinancial SOEs as public banks raise a different set of issues.

Guiding Principles

Countries should devise a strategy that prioritizes overall demands on fiscal resources, including support for SOEs. In providing support to SOEs, governments should consider a few guiding principles.

I. Prioritize between many demands

As public resources are scarce governments need to consider if support to specific SOEs is the best use of the limited budgetary resources. It may imply less resources for other critical areas such as health care. A cost-benefit analysis is needed considering the many demands and limited fiscal space. The analysis should include a review of the rationale for keeping the SOE. Potential costs should encompass immediate budgetary resources and possible future costs (e.g., risk from guarantees). At the outset, budget support should embed clear phasing-out mechanisms and limits or caps on the size of government risk exposure for certain interventions (e.g., credit or performance guarantees) should be established.

II. Target support to most systemically relevant SOEs

Fiscal support should be targeted on the most strategically and systemically relevant SOEs that face COVID-19 induced financial difficulties.⁵ This would limit budgetary cost and have the largest economic and social impact. For example, if lack of support to a public utility could endanger the provision of basic services (water, electricity), due to lack of alternative providers, it should get priority. This could apply to other sectors depending on the circumstances of the country (e.g., public transportation). For SOEs operating in competitive markets, governments should consider if private firms could assume a greater role in the provision of goods and services. In such cases, especially when budget resources are limited, the support to the SOE could be smaller (e.g., keeping more limited operations) or not given at all, with alternative support measures provided to workers.

A key consideration in providing support to SOEs is the degree of government ownership. If the government owns less than half the firm, then some restrictions (e.g., on dividend payments) may be warranted. In addition, in partially privatized SOEs that require a capital injection to stave off bankruptcy, appropriate burden-sharing between the state and private investors will need to be assessed.⁶

III. Equal treatment among SOEs and private competitors

The support should not be used to give preferential treatment (competitive advantage) to SOEs other private competitors could provide the goods and services. Preferably, the support should be the same available for the

⁵ It is difficult to establish comprehensive criteria a priori for what these SOEs are, but it would include firms whose closure would risk of disappearance of a whole ecosystem due to the SOE interconnectedness with the rest of the economy (e.g., electricity transmission companies).

⁶ For example, could consider liquidation with business continuity (e.g., Chapter 11 bankruptcy in the United States), that is, imposing haircuts on private creditors and shareholders and starting afresh.

entire sector unless an SOE has a clear policy mandate that requires different treatment. For example, the provision of a tax deferral to SOEs in manufacturing should be the same as provided to the sector in general.

IV. Transparency is imperative

A high level of scrutiny is critical to help ensure accountability and limit moral hazard. This is especially important if the support package is large, involves different financial instruments, and follows an exceptionally accelerated decision process. It should include ex post evaluation of the support to ensure accountability. A special framework may be necessary to ensure financial monitoring and fiscal risk oversight. This is particularly important if oversight was weak before the crisis. All types of support should preferably be approved by parliament and fully reported in budget and financial reports and information widely disseminated to the public.

Types of Measures

Policymakers should assess the strengths and weaknesses of various fiscal measures that may be available to deliver exceptional and temporary support to SOEs.⁷ The types of measures that can be soundly implemented vary depending on the financial health of the SOE (see below). Also, some measures can be implemented more quickly (cash flow relief) others may take more time (bringing in private investors). Moreover, the support should not be used to obfuscate past SOE problems. It will also be critical to limit fiscal risks.

Another key consideration is the immediate impact on the budget.⁸ Many governments may have limited room to provide cash and may need to consider other options. Moreover, existing mechanisms behind traditional types of support (e.g. subsidies, capital injections, guarantees) can be quickly used to help SOEs that are facing temporary or severe liquidity constraints due to the pandemic. SOE support during the crisis provides an opportunity to accelerate existing or introduce new structural reforms to improve SOE governance and performance. We next discuss some of the different options.

Options to strengthen cash flow of the SOE with an immediate impact on the budget. These require the government to be able to borrow, draw down liquid assets, or cut other expenditures to finance support to SOEs. The budget may be able to recover some of the support in the future.

- *Tax and social security contribution deferrals*, which mitigate liquidity pressures on SOEs at low cost, since the government can recoup tax later once the temporary COVID-19 shock subsides. However, in the interim the government loses revenue. These types of measures would usually be given to sectors of the economy and not just the SOE.
- *Subsidies* can be given to compensate for higher costs associated with policy mandates or when companies face greater financial distress (solvency risk).

Options to strengthen SOE balance sheet. These are especially useful for highly leveraged SOEs.

- *Equity injections* may be preferred to regular subsidies to deal with financial distress situations caused by shocks. This is especially the case in the context of mixed ownership as they allow the government greater participation in future recovery through dividends. However, the initial cash outlay could be prohibitive for cash strapped governments or imply higher government borrowing that could be too costly.

⁷ Several FAD notes summarize various types of government support that can be provided to private firms in the present crisis, some of which are also relevant for SOEs. See “[Public Sector Support to Firms](#)”; “[Expenditure Policies in Support of Firms and Households](#)”; “[Tax Issues: An Overview](#)”; and “[Public Banks’ Support to Households and Firms](#).”

⁸ Please see “[COVID-19: How to Record Government Policy Interventions in Fiscal Statistics](#).”

- *Debt-for-equity swaps* may be an option if the main source of financial pressures of the SOE is due to the debt service burden. However, the government's debt and debt-service will increase. Government could potentially recover some of the cost through future dividends.⁹

Options to facilitate SOE borrowing. They have limited or no immediate impact on budget or cash, but could imply significant fiscal risks.

- *Government guarantees* for SOE borrowing put the least pressure on current government finances. Guarantees should be temporary and limited.
- *On lending to SOEs.* This involves government borrowing directly in the market and on lending to SOEs—the government carries all the risks if SOE cannot repay. It may imply a lower cost of borrowing for the company than the option of using government guarantees in some cases.
- *Loans from public banks.* Public banks, if financially sound, can be used to provide support to SOEs that may have limited or no market access. If these operations result in losses to the public banks it will lead to lower dividends to government or need to re-capitalize the bank.¹⁰

Bringing private investors. Governments could bring strategic investors to the SOE. They could inject capital and bring expertise to help strengthen management of the company, though this needs to be done carefully to avoid fire sales during market nadirs.

Support Strategy by Financial Health of SOE

The decision on when and how to intervene will depend on the financial health of the company. Assuming the support is deemed necessary and in line with the guiding principles, governments will need to:

- assess the ability of the company to manage the shock without government support.
- monitor financial indicators of the company to help determine size and timing of support. If the support is deemed necessary, the government will need to closely monitor the evolution of the financial situation, including high frequency liquidity indicators.¹¹ It will better to act early before the company accumulates payment arrears (wages, suppliers).
- if the company has losses even before the crisis, understand the drivers (e.g., cost of quasi-fiscal activities, inefficiencies, mismanagement) and take necessary actions to limit potential risks.

Some examples:

SOE was profitable before the crisis and is expected to remain so once the crisis subsides. These enterprises may require temporary support during the crisis. In these cases, governments may want to give support to the SOE to ensure continuation of services provided by the company and preserve its value—assuming in line with the guiding principles. However, before considering fiscal support, the company should be asked to exhaust other means of managing the turbulence (e.g., Ethiopian Airlines is taking advantage of its financial strength to avoid government support). For example, some will retain the capacity to borrow. Others may be able to sell non-core assets or postpone investments. Also, dividends or royalty payments to the government could be temporarily reduced or delayed.¹² Once these possibilities are exhausted, government

⁹ When the government assumes the debt of an SOE owed to a third party, the government may want to seek a net present value discount on the loan as the third party's claim is now on the government rather than likely less credit worthy SOE.

¹⁰ The loans should be designed with appropriate safeguards and be transparent to ensure accountability and contain fiscal costs. See note on "[Public Banks' Support to Households and Firms.](#)"

¹¹ This would require an effort to collect data at higher frequency. For example, are payables becoming excessive in comparison to historical trends and to expenditures? Is there a quick degradation of cash availability of the SOE's bank accounts over the recent weeks? (periodicity: weekly); Is there an accumulation of arrears or payment delays to the SOE's contractors over the recent weeks (periodicity: biweekly); Re-evaluation of fixed assets (periodicity: monthly).

¹² For example, oil companies, if well managed, can usually weather on their own significant turbulence.

support could be primarily through tax deferrals or government guarantees (which have limited immediate impact on the budget). However, larger support may be needed in the sectors most hit by the pandemic.

SOE has low debt but is dependent on regular transfers from the budget to cover costs associated with policy mandates. Support may be required for quasi-fiscal activities, like subsidized or below cost prices, or overemployment. It could involve traditional forms of support such as increasing subsidies directed to cover public mandates, or capital injections. In some cases, if cash constrained, the government could also consider guaranteeing loans to the SOE or other forms of support.

The support should be accompanied by measures to contain costs. One issue is that moral hazard concerns may have some relevance if it is difficult to distinguish effects of the crisis from other factors driving the losses. For example, the SOE's financial difficulties could be related to rising costs of quasi-fiscal activities, but may reflect inefficiencies and mismanagement. As such, the support may need to include a strategy to improve efficiency and contain costs (wages). Governments could also consider revising policy mandates, for example allowing the company to raise prices closer to costs (could be done gradually), to contain fiscal costs and risks.

SOEs with systematic and large losses, weak balance sheets. These are the cases likely involving the largest costs to the budget and could persist well beyond the crisis. A triage would be important:

- firms that are not viable and do not have a critical policy mandate should be sold or closed. Governments may need to provide temporary support for workers. For example, firms in sectors where there is private competition that provides goods and services at competitive prices (e.g. manufacturing, retail) have less reason to exist.¹³
- for strategic or systemically important firms—that meet the guiding principles—support should be accompanied by a substantial reform package. It may also require developing a strategy to deal with quasi-fiscal activities. Such reforms will likely take time. For example, Jordan reformed the electricity company, NEPCO, substantially reducing the operational losses that were a large burden on the budget (see Annex 3). This could involve support from donors, such as the case of the Gambia National Water and Electricity Company (NAWEC) (Annex 3). To limit costs and bring expertise, consideration could also be given to bringing in private partners.¹⁴

III. ENHANCED GOVERNANCE AND OVERSIGHT

Governance Considerations around the Support Package

The determination of whether, how, and to what extent support should be provided to SOEs needs to take into account a number of critical governance factors. The approval and execution of the support measures should also be conducted in a fully transparent manner.

- **In the immediate term, there should be full transparency on all support and conditions attached.** Any support provided to SOEs should be approved by parliament and reported in budget documents (including below-the-line operations, use of extrabudgetary funds, or contingent liabilities). If it involves support by public

¹³ For example, when national airlines are a large burden to the budget and there are private alternatives, governments should assess if it is worth saving the company. For example, South Africa recently announced it will not provide additional support to South African Airways. The government is exploring various options and, if necessary, the airlines will close.

¹⁴ For example, in 2011–12, the Seychelles government, as a part of the restructuring of the national airline, which included a capital injection and assumption of the airline liabilities and restructuring costs by the government (about 4.5 percent of GDP), sold a 40 percent stake in the airline to Etihad Airways.

banks, costs, and risks should be made public (see note on public banks). Costs and risks of all operations should be disclosed regularly.

- **Beyond this, there should also be more meaningful and lasting reforms.** The provision of support in the immediate term needs to be accompanied by a commitment to medium- and longer-term reforms that will address the financial viability of the SOEs including, where needed, exiting some activity where appropriate. SOEs are also often used as a vehicle to deliver quasi-fiscal activity. Where these activities are a significant contributor to SOE under-performance, consideration needs to be given to transitioning them from the SOEs to the government budget.

Broader Oversight and Governance Efforts

Given widespread governance weaknesses involving individual SOEs and the SOE sector as a whole, it will be important to bolster controls and transparency.

- **Effective oversight of the SOE sector and a strong ownership function.** There needs to be a strong SOE ownership function in government along with effective arrangements for oversight, with clearly demarcated roles for the ministry of finance, the sectoral ministries, and where they exist the SOE oversight body such as the SOE bureau or commission. All countries should be encouraged to publish a comprehensive annual report on the overall SOE sector (e.g., Angola, Ghana, Liberia). Where support is provided to SOEs in response to the crisis, beneficiary SOEs will need to be subject to enhanced monitoring and oversight in the short term.
- **SOE financial transparency and accountability.** Individual SOEs should produce and publish audited financial statements within a limited time after the close of the fiscal year. In addition, SOE balance sheets should be reviewed and major assets revalued periodically. Financial support to SOEs with qualified audit statements should be avoided. SOEs receiving support should be required to publish their most recent audited financial statements as a pre-condition for receiving such support.
- **Corporate governance.** The need for government support creates an opportunity to strengthen corporate governance to ensure appropriate use of public resources. Minimum corporate governance standards need to be put in place to ensure that the responsibilities of boards of directors are clear, that arrangements are in place for measuring, monitoring, and assessing SOE performance, and that boards of directors are held accountable for performance including through the use of performance contracts and/or service agreements.
- **Strengthening fiscal risk management.** All SSA countries should be encouraged to progressively strengthen their identification, management, and disclosure of fiscal risks including (Annex 2).
- **Updating legal frameworks.** In many countries, SOEs operate under an outdated or ineffective legal framework. The sector needs a modern legal framework to govern its operations, including with a clear definition as to what constitutes an SOE, given that many countries either do not have a complete list of their SOEs or are unclear about whether some entities are SOEs or government units.

IV. DIAGNOSTIC TOOLS AND CAPACITY DEVELOPMENT

The IMF has many tools at its disposal that can help countries improve the finances of their SOE sector:

- Compiling the PSBS to take stock of the size of the SOE sector and its impact on the overall finances of the public sector.
- Conducting either a full Fiscal Transparency Evaluation (FTE) to assess transparency practices, identify gaps, and develop an action plan to address these, or Fiscal Risk Assessment.
- Conducting an SOE Health Check, to assess financial strength of individual SOEs and the sector as a whole.
- Assessment of guarantees to estimate the extent of fiscal exposure.
- Applying an SOE stress test to determine the of different macroeconomic assumptions and scenarios.

The IMF can also provide CD to help countries enhance monitoring, control and risk mitigation in relation to the SOE sector. Such CD could help with:

- Updating the legal framework on SOEs
- Strengthening SOE oversight arrangements and fiscal risk management capacity in ministries of finance
- Completing budget documentation (e.g., fiscal risk statements, dedicated budget documentation on SOEs)
- Strengthening budget preparation and execution to (1) better reflect SOE financial relations with the central government budget and (2) implement standard budget and accounting procedures and tools
- Ensuring adequate control and reporting through modernized budget classification and chart of accounts, financial information systems, and periodic fiscal reports compliant with international standards
- Strengthening capabilities to conduct spending reviews, to help with expenditure reprioritization and rationalization

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ANNEX 1. FINANCIAL CHALLENGES FACED BY SOEs

Even before the COVID-19 crisis, the sector was experiencing financial difficulties. Many SOEs were in a weak financial position prior to the current pandemic. These entities were loss-making, heavily indebted, seriously illiquid, had large amounts of unpaid bills, and were heavily reliant on government transfers for their survival. In South Africa, debt of a single company (ESKOM, the electricity company) is about 10 percent of GDP of which 80 percent is guaranteed by government, and the company's direct cost to the budget has exceeded 9 percent of GDP since 2008/9. In Zimbabwe, many SOEs have run losses over the years, accumulating about 2.8 percent of GDP from 2011 to 2014. This has resulted in government transfers to the sector totaling 7.8 percent of GDP. In some countries, SOEs have benefited from government guarantees, which now pose fiscal risks to the state.

SOE finances in SSA commonly have heavy interlinkages between themselves, public banks, and the government, with large cross holdings of assets and liabilities, particularly arrears. There are many examples of bills between SOEs and the government going unpaid, resulting in balance sheet problems throughout the economy. Where these cross holdings exist, financial or liquidity challenges faced by one part of the public sector could cascade through the rest of the public sector, as has been illustrated by stress tests done by the IMF in some countries. In The Gambia, defaulted crossholdings resulted in NAWEC being unable to service its debt to the banking sector, causing the supporting government guarantee to be called.

The financial position and performance of some SOEs are affected by the extent to which they provide quasi-fiscal activity. Some SOEs are conduits for quasi-fiscal activity, such as electricity companies whose tariffs do not reflect the cost of production or airlines operating unprofitable routes for social purposes. These SOEs are generally not compensated for these activities, with attendant implications for their financial performance. When this continues unchecked, it has resulted in the SOEs becoming dependent on regular transfers from the budget to cover their losses or accumulation of expenditure arrears by the SOEs with spillover into the broader economy. In Madagascar, the highly indebted JIRAMA (electricity and water utilities) received about 1.1 percent of GDP in subsidies from the government in 2014. In extreme cases, the SOE has to be closed or privatized. The Cape Verdean national airline, TACV, is a case in point which ended up being privatized. SAA is another example, but still in state ownership.

Some SOEs do have the potential to be profitable and make a positive contribution to the economy as a whole. While much of the IMF's work on this topic to date has necessarily focused on situations where the SOE sector is facing challenges, there are examples of SOEs that are well managed, profitable, and can add value in the economy. In Seychelles, most SOEs are low risk, viable companies contributing about 0.5 percent of GDP in net transfers to the budget in 2018. For this reason, FAD advice has been for countries seeking to reform their SOE sector to conduct a review of the status of each SOE aimed at identifying those that are of high policy and strategic importance and are also commercially viable. Those meeting these criteria could be retained and closely monitored to ensure that they make a positive contribution to the economy, while others should be reformed to stem their drain on the public finances.¹⁵

¹⁵ IMF. 2016. "How to Improve Oversight of Public Corporations."

ANNEX 2. FISCAL RISKS FROM SOEs – LESSONS FROM FISCAL TRANSPARENCY EVALUATIONS

FTEs conducted on six SSA countries indicate that transparency of fiscal risks from SOEs is relatively basic. FAD has conducted FTEs for six SSA countries of which four have been published.¹⁶ Most of these countries disclose information on transfers to SOEs in the annual budget documentation (e.g., parastatal annex in Kenya) and the annual financial statements. However, these documents have omissions (e.g., incomplete SOE portfolio in Senegal or absence of information on indirect transfers in Mozambique) or are uneven and delayed due to difficulties in consolidating data (e.g., Uganda submission of financial statements to the Accountant General). Moreover, analysis of SOE debt and fiscal performance indicators is scant or nonexistent.

The absence of comprehensive and detailed reporting and monitoring is worrisome as the financial performance of many SOEs creates significant fiscal risks for the government. Poor financial performance by SOEs has necessitated calls on the budget in terms of subsidies, capital injections and on-lending. In Kenya, public corporations have benefited from government support in the form of on-lent and guaranteed loans (equivalent to 4.6 percent of GDP). A number of these loans have not been repaid or are in arrears.

Table 1. Summary Assessment of SSA FTEs for the Dimension on SOEs

Countries	Assessment of practices	Importance of Fiscal risk
Kenya	Basic: Consolidated financial statements are produced for PCs and SAGAs. An annex to the budget presents fiscal flows between the government and PCs.	High: Financial risk is concentrated in ten public corporations, which account 95 percent of all loss making entities and 84 percent of entities with negative equity.
Mozambique	Basic: All direct transfers between the government and public corporations are disclosed on at least an annual basis.	Medium: Fiscal risks resulting from financial performance of public corporations are not assessed.
Senegal	Basic: The key transfers between general government and public enterprises are disclosed on an annual basis, but government shareholding policy is not published.	High: Public enterprises are an important part of the economy and pose substantial fiscal risks that may already have materialized.
Uganda	Basic: Transfers to public corporations are disclosed but there is no reporting of the financial performance of the sector.	Medium: Public corporations are largely profitable, but the Bank of Uganda has needed recapitalization.

Source: Published FTEs.

The FTEs also underline the lack of reporting and monitoring of SOEs despite the financial costs and fiscal risks they represent. Strengthening these weaknesses would help be better prepared to manage shocks to SOEs, like during the pandemic, and mitigate potential costs to the budget. For example, the FTEs highlight:

- SOEs are generally outside the scope of fiscal reports and statistics (FTE Pillar I: Coverage of Institutions) and budget documentation and information on SOEs are generally incomplete (Pillar II: Budget Unity). Budget execution reports as well as annual consolidated financial statements mostly focus on central government even though SOEs may be significant. For instance, Uganda’s financial statements cover central and local governments although public corporations account for about 32 percent of government’s assets and liabilities.
- Extending the coverage of country balance sheets from central government to public sector shows the true scale of liabilities (Pillar I: Coverage of Stocks). Inclusion of SOE liabilities gives a more extensive image of public sector liabilities than usually reported. In Kenya, public sector liabilities estimated by the 2014 FTE amounted at 93 percent of GDP, more than double the reported level of public debt. This included liabilities of noncommercial parastatals (4.2 percent of GDP) and of commercial SOEs (21.6 percent of GDP).
- Information and monitoring of government guarantee to SOEs, whether explicit or implicit, are scarce (Pillar III: Guarantees). Reported stocks of explicit guarantees to SOEs are often inexistent or incomplete even though they pose significant fiscal risks (e.g., international loans guaranteed to seven SOEs amounted to 0.9 percent of GDP in Kenya).

¹⁶ The FTEs for Rwanda (2019) and Tanzania (2015) are yet to be published, as well as the FTE update for Mozambique (2020). Published FTEs include Kenya (2014 and 2019), Mozambique (2014), Senegal (2018), and Uganda (2017).

ANNEX 3. EXAMPLES OF REFORMS

Rescuing a Systemically Important Utility Company – The Gambia’s NAWEC

In The Gambia, NAWEC is the monopoly electricity and water utility and is entirely state-owned. The company has a long history of accumulated losses and mounting debts. These debts included borrowing from banks which had to be restructured into a government guaranteed bond on which NAWEC subsequently defaulted resulting in the guarantee being called.

In March 2018, the Ministry of Finance and Economic Affairs (MoFEA) signed an MOU with NAWEC aimed at restructuring the company’s debt and improving its future viability. Based on that MOU, GMD 7.2 billion (US\$154 million) of NAWEC’s long term debt was transferred to the Government or converted to equity. At the same time, the MoFEA assumed responsibility for paying NAWEC’s debts accumulated through a short-term credit facility used to finance fuel imports for electricity generation. Total liabilities assumed or capitalized by the Gambian Government represented 78 percent of NAWEC’s total debt, accounting for 9.3 percent of 2018 GDP.

	2018	
	GMD Millions	USD Millions
March 2018 Bailout		
Loan assumed by the MoFEA	2,911.4	62.3
o/w Owing to the Social Security Fund	816.7	17.5
Bonds assumed by the MoFEA	1,686.4	36.1
Government loans capitalized	2,645.9	56.6
Short-term commercial debt	253.0	5.4
Total	7,496.8	160.4
Percent of Total NAWEC Debt	78	
Percent of GDP	9.3	

With World Bank support, the following prior actions were agreed for restructuring NAWEC and improving governance and financial performance in the company:

- A time-bound financing plan approved by MoFEA to settle cross-arrears between the public sector and NAWEC as of June 2019.
- Centralization of payments to NAWEC for the electricity bills of critical public facilities (hospitals, the military, and street lighting) and remaining current on these bills.
- Starting the transitioning of non-critical public sector customers to prepaid meters.
- Restructuring approximately 75 percent of NAWEC’s debt as per the March 2018 MOU.
- Publication of a new tariff methodology including a mechanism for compensating NAWEC for any shortfall between the tariff and required revenues starting in 2019.
- Approval by the NAWEC Board of a 2019-25 Strategic Development Plan for the company.
- Signing by MoFEA of a full performance contract for NAWEC for 2020 with incentives to meet key operational and financial performance indicators based on the business plan.
- Approving a new Board Charter for NAWEC to reinforce the independence of directors.
- Appointing new directors to NAWEC per the new organigram.

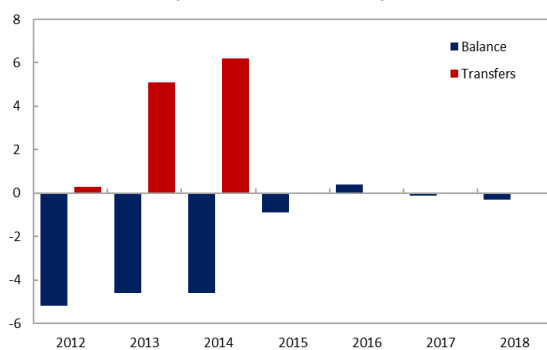
Reform of Jordan’s electricity company

The reform of Jordan’s state-owned electricity company, NEPCO, illustrates how governments can reduce significantly the burden on the budget. Subsidies to NEPCO were close to 6 percent of GDP in 2014, a large number especially when compared to the share of total health spending that stood at 7.5 percent of GDP in the same year (WHO). The company losses also put a significant pressure on the government at a time public debt

was already high. The reform of NEPCO involved a broad strategy including: (1) gradual tariff adjustments since 2012; (2) the installation of a liquified natural gas plant to switch the primary source of energy from fuel to gas; and (3) vulnerable households were supported by increasing cash transfers. As a result, public transfers to NEPCO were eliminated as of 2015, and NEPCO has posted small positive and negative net operational balances since 2016 (Figure 2).

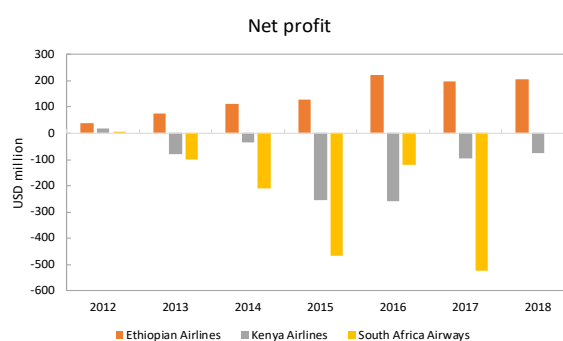
Despite the significant improvements, it will be important to continue efforts to consolidate the gains and address remaining challenges. For example, one issue is the cross-subsidization of untargeted electricity subsidies to households by charging businesses high tariffs. Businesses in turn have reduced their consumption from the grid and invested in self-generation capacity. Another challenge will be addressing the cost of an oil-shale power purchase agreement with an estimated cost of 0.7 percent of GDP annually.

Figure 2. Performance of NEPCO (Percent of GDP)



Source: IMF staff reports and authorities

Figure 3. National Airlines in Africa Have Very Different Performance



Note: Refers to fiscal years, which vary across countries.

Experience with National Airlines in Africa

Several countries on the continent have state-owned airlines, but only few have been successful. As flag-carriers they are often seen as a sign of prestige as well as a tool for marketing the country. Ethiopian Airlines has been a success story. Some of the factors that contribute to its success include:

- Good business model. It benefits from geographic location, built a good network; keeps maintenance costs under control; and safety has been a priority.
- The company has also been focused on continually improving its internal processes, the customer experience and the quality of its human capital. It has been able to successfully contain employment costs and continually seeks to achieve cost savings in other areas.
- It has been able to keep leverage lower than many other airlines, providing it with the financial flexibility to absorb shocks.

In contrast, many other airlines in Africa, but also internationally, struggle financially, often requiring governments to divert capital from other important developmental priorities to recapitalize the airline. Examples include Kenyan airlines and SAA. In addition, many African airlines operate routes which are unprofitable. While promoting connectivity may generate a positive externality through enabling trade and tourism, this is not internalized by the airline and its financial position deteriorates. Repeated losses erode the equity position of the airline, reduce its ability to withstand risks, and can eventually result in the airline becoming insolvent and the government having to provide a recapitalization. For example, since 2011, SAA has not turned a profit and has relied on bailouts from the government. These have amounted to 20 billion rands (or just shy of US\$1.1 billion) in the last three years.

Air Seychelles is another example of a government-owned airline that continues to struggle despite government support. After a restructuring in 2011–12, Air Seychelles enjoyed several years of profitability. However, it turned in a significant loss during 2017–18. Air Seychelles subsequently embarked on a comprehensive operational restructuring, including staff redundancy and the closure of loss-making international routes, with financial support from its shareholders. The government of Seychelles owns 60 percent of the company while Etihad Airways owns the rest. Etihad wrote off 2.3 percent of GDP of Air Seychelles' debt and agreed to convert 2 percent of GDP of its current liabilities into preference shares. The government's assistance consists of guarantees equivalent to 2.4 percent of GDP from 2019–24 and 0.4 percent of GDP in grants in 2019.

**Figure 4. Evolution of Capacity among Airlines
(Number of passengers, thousands)**

